Supreme Court of the United States

OCTOBER TERM, 1965

No. 351

COMMISSIONER OF INTERNAL REVENUE, PETITIONER

vs.

WALTER F. TELLIER, ET UX.

ON WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE SECOND CIRCUIT

INDEX

[fol. A]

IN THE UNITED STATES COURT OF APPEALS FOR THE SECOND CIRCUIT

No. 28823

WALTER F. TELLIER AND EVELYN H. TELLIER, PETITIONERS

against

COMMISSIONER OF INTERNAL REVENUE, RESPONDENT

On Petition for Review of the Decision of the Tax Court of the United States

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EXCERPTS FROM APPENDIX TO PETITIONERS BRIEF—filed May 28, 1964

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* * * *

[File Endorsement Omitted]

[fol. 1]

DOCKET ENTRIES

BEFORE THE TAX COURT OF THE UNITED STATES

Docket No. 90189

Date	Filings and Proceedings
Dec. 6, 1960	Petition Filed: Fee Paid Dec. 6, 1960
Dec. 6, 1960	Request by petr. for trial at New York, New York
Feb. 3, 1961	Answer by resp. filed
Feb. 3, 1961	Request by resp. for trial at Newark, N. J.
Feb. 28, 1961	Reply filed by Petr.
Dec. 19, 1961	Notice of trial at New York, New York, March 19, 1962

Date	Filings and Proceedings
Mar. 2, 1962	Motion by petr. for continuance from March 19, 1962 trial calendar at New York, N. Y.
March 5, 1962	Notice of Hrg. March 19, 1962 New York, N. Y. on Petr's motion for continuance.
March 19, 1962	Hrg. before Judge Forrester—New York (Newark Session)
	Petr's Written Motion for Continuance—Granted
	Continued Generally.
March 29, 1962	Transcript of Hrg. March 19, 1962 rec'd
July 24, 1962	Notice of trial at New York, New York; Oct. 29, 1962
[fol. 2]	
Nov. 8, 9, 1962	Trial before Judge Scott—New York, N. Y. (Newark)
	Resp. Amendment to Answer filed and served 11/9/62
	Resp. Motion to Amend Answer (Obj. by Petr) Granted
	Resp. granted leave to Reply.
	Stip. of facts w/jt. exhibits
	Briefs due 1/8/63
	Reply Briefs due 2/25/63
	Submitted to Judge Scott
	Under Submission
Dec. 5, 1962	Reply to Amended Answer filed by petitioners.
Dec. 7, 1962	Transcript of proceedings of Nov. 8, 9, 1962 received. (1)
Dec. 21, 1962	Motion by petr. for extension of time to February 25, 1963 to file Brief and to March 27, 1963 to file Reply Brief.

Date	Filings and Proceedings
Jan. 8, 1963	Motion by resp. to Amend Amendment to Answer filed.
	Amendment to Amendment to Answer lodged.
Jan. 14, 1963	Amendment to Amendment to Answer filed
[fol. 3]	
Feb. 12, 1963	Reply to Amendment to Amendment to Answer filed.
Feb. 12, 1963	Brief for Petrs filed
Feb. 25, 1963	Motion by resp. for extension of time from Feb. 25, 1963 to March 11, 1963 to file Brief.
March 11, 1963	Brief for Respondent filed
Apr. 19, 1963	Motion by petr. for enlargement of time to May 15, 1963 to file Reply Brief.
May 13, 1963	Reply Brief for Petr. filed
May 15, 1963	Reply Brief for Resp. filed
Aug. 14, 1963	Memorandum Findings of Fact and Opinion filed Judge Scott
	Decision will be entered under Rule 50
Nov. 14, 1963	Agreed Computation filed and Dec.
Nov. 21, 1963	Decision entered, Judge Scott
	Appellate Proceedings
Feb. 17, 1964	Stipulation for Venue filed.
Feb. 17, 1964	Petition for Review by USCA 2nd Cir. filed by petrs.
Feb. 17, 1964	Notice of Filing Petition for Review to Both Parties filed, with proof of service thereon by resp.
Feb. 17, 1964	Notice of Date of Transmission of Record to Both Parties.

[fol. 4]

T. C. Memo. 1963-212

BEFORE THE TAX COURT OF THE UNITED STATES

Docket No. 90189

WALTER F. TELLIER AND EVELYN H. TELLIER, PETITIONERS

v.

COMMISSIONER OF INTERNAL REVENUE, RESPONDENT

EXCERPTS FROM MEMORANDUM FINDINGS OF FACT AND OPINION—filed August 14, 1963

Michael Kaminsky, for the petitioners.

Laurence Goldfein, for the respondent.

SCOTT, *Judge*: Respondent determined deficiences in petitioners' income taxes for the years and in the amounts as follows:

Year	Deficiency
1952	$26,965.96
1953	30,955.12
1954	31,938.86
1955	44,741.71
1956	2,227.31

The issues for decision are: (1) whether the gains realized by petitioners on the sale of certain securities constitute ordinary income or capital gains, and (2) whether legal expenses incurred and paid by one of petitioners in

[fol. 5] the unsuccessful defense of a criminal prosecution are deductible.

FINDINGS OF FACT

Some of the facts have been stipulated and are found accordingly.

Petitioners, husband and wife now residing in Rye, New York, filed a joint Federal income tax return with the district director of internal revenue, Lower Manhattan, New York for the calendar year 1952 and filed joint Federal income tax returns with the district director, Newark, New Jersey, for the calendar years 1953, 1954, 1955 and 1956. On each of these returns the occupation of Walter F. Tellier (hereinafter referred to as petitioner) was shown as "Security dealer."

* * * *

[fol. 6] * * *
[fol. 7]

* * * *

During the period January 1, 1952 to May 11, 1956 petitioner was the controlling and principal participant in the business conducted under the name Tellier and Company. After May 11, 1956 and for the remainder of 1956, petitioner continued the business of Tellier and Company individually under that name. At all times petitioner exercised complete control over the policy and management of Tellier and Company and the other participants performed only those functions assigned to them by petitioner which included the supervision of employees who worked directly under them.

Tellier and Company was registered with the Securities and Exchange Commission as brokers and dealers in securities, and petitioner and Tellier and Company maintained places of business during the years here involved at 1 Exchange Place, Jersey City, New Jersey and at 42 Broadway, New York, New York.

At all times material hereto Tellier and Company acted as an underwriter in the public sale of stock offerings of corporations and purchased corporate securities for resale to customers with the purpose of deriving a profit on

the spread between the purchase and sales prices. Included in the securities purchased by Tellier and Company for resale were securities which had been distributed through its underwriting activities. In many instances Tellier and Company acted as underwriters in the public sale of securities of corporations starting new businesses with capital entirely raised by an initial public sale of capital stock. Tellier and Company also acted as a broker or agent in the sale of securities and the profits it derived from this function were in the form of commissions.

[fols. 8-19] * * *

[fol. 20]

* * * *

Petitioner was tried and convicted upon a thirty-six count indictment charging him with violations of the fraud section of the Securities Act of 1933, 15 U.S.C. section 77(q)(a); with violations of the mail fraud statute, 18 U.S.C. section 341; and with conspiracy to violate each of those statutes, 18 U.S.C. section 371.

Petitioner on April 12, 1957 received concurrent sentences of 4½ years of imprisonment on each count and was fined a total of $18,000 as a result of the criminal conviction referred to above.

In connection with the unsuccessful defense of this criminal prosecution, petitioner in 1956 incurred and paid legal expenses in the amount of $22,964.20 and claimed a deduction for such amount as a business expense. Respondent disallowed the claimed deduction.

[fol. 21]

* * * *

OPINION

* * * *

[fols. 22-28] * * *

[fol. 29]

* * * *

The second issue is whether legal expenses incurred and paid in the unsuccessful defense of a criminal prosecution are deductible. The Courts have long held that such expenses are not deductible and one of the reasons for the

disallowance of such deductions has been that their allowance would frustrate clearly defined public policy. *Burroughs Bldg. Material Co.* v. *Commissioner*, 47 F. 2d 178 (C.A. 2, 1931) affirming 18 B.T.A. 101; *Anthony Cornero Stralla*, 9 T.C. 801 (1947); *Thomas A. Joseph*, 26 T.C. 562 (1956); *Henry L. Peckham*, 40 T.C. —— (May 15, 1963) on appeal (C.A. 4, July 10, 1963). See *Commissioner* v. *Heininger*, 320 U.S. 467 (1943); and Cf. *Tank Truck Rentals* v. *Commissioner*, 356 U.S. 30 (1958).

Petitioner argues that the recent Supreme Court opinion of *Gideon* v. *Wainwright*, 372 U.S. 335 (1963), indicates a public policy of providing legal counsel for defendants in criminal actions and therefore petitioner asserts it should not be inferred that Congress intended to withhold a tax deduction for those employing counsel in defending criminal prosecutions. There is no question that it is in the public interest that defendants have counsel in crimi- [fol. 30] nal prosecutions and that it has been held to be a constitutional right secured by the sixth and fourteenth amendments. The fact that an expenditure is in connection with a constitutionally guaranteed right does not require the conclusions that the amount so expended is deductible as an ordinary and necessary business expense. *Cammarano* v. *United States*, 358 U.S. 498 (1959). Even though the payment of legal fees in the unsuccessful defense of a criminal prosecution may not be as proximately related to the illegal activity as the payment of the fines and penalties involved in the *Tank Truck Rentals* case, such legal expenses flow from the illegal acts.

Petitioner claims *Longhorn Portland Cement Co.*, 3 T.C. 310 (1944) supports his position. In that case we allowed deductions for payments made in compromise of a State antitrust action brought against the taxpayer and for the legal fees relative to the action. However, in *Longhorn Portland Cement Co.*, *supra*, we pointed out that the taxpayer was not proven guilty of the alleged antitrust violations, that the court's judgment in the antitrust action specified that the settlement agreement was not to be construed as an admission of guilt, and further that the taxpayer entered into the settlement rather than assert its innocence for sound business reasons. Petition-

er in the instant case was tried and found guilty of the illegal acts with which he was charged. Cf. *Henry L. Peckham, supra.*

We sustain respondent in his disallowance of petitioner's claimed deduction for legal fees paid in the unsuccessful defense of a criminal prosecution.

Other issues raised by the pleading have been disposed of by agreement of the parties.

Decision will be entered under Rule 50.

[fol. 31]

BEFORE THE TAX COURT OF THE UNITED STATES

Docket No. 90189

WALTER F. TELLIER AND EVELYN H. TELLIER, PETITIONERS

v.

COMMISSIONER OF INTERNAL REVENUE, RESPONDENT

DECISION—Entered November 21, 1963

Pursuant to the opinion of the Court filed August 14, 1963, and the agreed computation of the tax liabilities filed by the parties; and incorporating herein the facts recited in the computation as the findings of the Court, it is

ORDERED and DECIDED: That there are deficiencies in income tax due from the petitioners for the taxable years

1952 through 1956 in the respective amounts of $26,965.96, $30,955.12, $33,052.78, $44,741.71, and $2,227.31.

(Signed) IRENE F. SCOTT
Judge

Entered Nov 21 1963

* * * *

It is hereby stipulated that the foregoing decision includes an increased deficiency in income tax in the amount of $1,113.92 for the taxable year 1954, claim for which [fol. 32] the respondent makes pursuant to the provisions of § 6214(a) of the Internal Revenue Code of 1954.

It is further stipulated that the foregoing decision is in accordance with the opinion of the Court and the agreed computation of the parties, and that the Court may enter this decision without prejudice to the right of either party to contest the correctness of the decision entered herein, pursuant to the statute in such cases made and provided.

MICHAEL KAMINSKY
Counsel for Petitioners

(Signed) R. P. Hertzog
FXG

R. P. HERTZOG
ACTING CHIEF COUNSEL
INTERNAL REVENUE SERVICE

[fol. 33]

IN THE UNITED STATES COURT OF APPEALS
FOR THE SECOND CIRCUIT

No. 29—September Term, 1964.

Argued October 8, 1964

Docket No. 28823

WALTER F. TELLIER AND EVELYN H. TELLIER,
PETITIONERS

v.

COMMISSIONER OF INTERNAL REVENUE, RESPONDENT

OPINION—February 16, 1965

Before:

LUMBARD, *Chief Judge*,
HAYS and ANDERSON, *Circuit Judges*.

Petition for review of a decision of the Tax Court, Scott, *Judge*, T. C. Memo. 1963-212, 22 CCH Tax Ct. Mem. 1062, insofar as that decision found that income from the sale of certain securities was taxable as ordinary income because the securities were held for sale to customers in the ordinary course of business, Section 117 (a) (1) (A) of the Internal Revenue Code of 1939 (Section 1221 (1) of the 1954 Code).

Affirmed as to this issue.

[fols. 34-35] * * *

[fol. 36]

* * * *

HAYS, *Circuit Judge* (with whom Chief Judge Lumbard, Judges Waterman, Friendly, Smith, Kaufman, Marshall and Anderson concur):

II.

The second issue presented in this case is whether legal expenses for the unsuccessful defense of a criminal action are deductible. We have decided that this problem, though [fol. 37] long considered as authoritatively answered in this Circuit, should be reexamined.[3]

Taxpayer was tried and convicted on a thirty-six count indictment charging him with violations of the fraud section of the Securities Act of 1933,[4] with violations of the mail fraud statute,[5] and with conspiracy to violate these statutes.[6] He was sentenced to four and one-half years of imprisonment on each count, the sentences to run concurrently, and was fined $18,000. He claimed a deduction in 1956 in the amount of $22,964.20, representing expenditures during that year incurred in his defense in the criminal proceeding. The Commissioner disallowed this deduction and his ruling was sustained by the Tax Court.

In disallowing a deduction for the expenses of an unsuccessful defense of a criminal action the tax authorities are following a purely judge-made rule. There is nothing in the statute which dictates or even suggests such a result. The applicable provision is Section 162 of the 1954 Code which provides:

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[3] After the appeal on this issue was heard by a panel consisting of Chief Judge Lumbard and Circuit Judges Hays and Anderson, the qualified judges of this Court agreed that the appeal should be considered *en banc*.

The appeal brought into question a principle which heretofore had been well settled by a prior decision of this Court. It was felt that we should reverse a previous categorical ruling of the Court only by vote of all the qualified circuit judges considering the question *en banc*.

[4] § 17, 48 Stat. 84 (1933), as amended, 15 U. S. C. § 77q(a) (1958).

[5] 18 U. S. C. § 1341 (1958).

[6] 18 U. S. C. § 371 (1958).

> "There shall be allowed as a deduction all the ordinary and necessary expenses paid or incurred during the taxable year in carrying on any trade or business . . ."

There is no provision which expressly prohibits the deduction of the expenses of an unsuccessful defense. The general prohibition on deductions, Section 262, reads:

[fol.38] "Except as otherwise expressly provided in this chapter, no deduction shall be allowed for personal, living, or family expenses."

That the framers of the legislation did not intend that it should be used for moral reform is indicated by the following bit of legislative history: In the Senate debate over the provision with respect to business losses, objection was raised to its liberality. It was suggested that deductions for losses be permitted only when incurred in a "legitimate" trade or business. The suggestion was rejected. Senator Williams, who was in charge of the income tax sections of the bill, explained that the object of the bill was

> "to tax a man's net income; that is to say, what he has at the end of the year after deducting from his receipts his expenditures or losses. It is not to reform men's moral characters, that is not the object of the bill at all. The tax is not levied for the purposes of restraining people from betting on horse races or upon 'futures,' but the tax is framed for the purpose of making a man pay upon his net income, his actual profit during the year." 50 Cong. Rec. 3849 (1913).

In 1951 Congress rejected a proposal for disallowing deductions under Section 162 "for any expense paid or incurred in or as a result of illegal wagering" on the ground that the Internal Revenue Code was not intended to penalize or prohibit unlawful activities.[7]

Randolph Paul said:

> "As exploration of relevant Congressional debates indicates, Section 23(a)(1)(A) [Section 162(a)] is

[7] 97 Cong. Rec. 12230-44 (1951).

not an essay in morality, designed to encourage vir-
[fol. 39] tue and discourage sin. It 'was not contrived as an arm of the law to enforce State criminal statutes by augmenting the punishment which the State inflicts.' Nor was it contrived to implement the various regulatory statutes which Congress has from time to time enacted. The provision is more modestly concerned with 'commercial net income'—a businessman's net accretion in wealth during the taxable year after due allowance for the operating costs of the business. . . . There is no evidence in the Section of an attempt to punish taxpayers . . . when the Commissioner feels that a state or federal statute has been flouted. The statute hardly operates 'in a vacuum,' if it serves its own vital function and leaves other problems to other statutes. When Congress has wished to deny tax deductions as a means of reinforcing the sanctions of other federal statutes, it has done so deliberately and explicitly." [8]

No Supreme Court case lends any support to the rule that the legal expenses of an unsuccessful criminal defense when paid or incurred in connection with the carrying on of a trade or business are not deductible. In fact the Court has cast doubt on the rule by what it has said with respect to the reasons ordinarily given to justify the existence of the rule. These reasons are: first, that the expenses occasioned by unlawful activities are not ordinary and necessary in the conduct of a business [9] and sec-
[fol. 40] ond that the allowance of a deduction for such expenses would be contrary to public policy.[10]

Of the legal expenses of resisting issuance by the Postmaster General of a fraud order, the Court said in *Com-*

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[8] *The Use of Public Policy by the Commissioner in Disallowing Deductions,* Proceedings Tax Inst. Univ. of So. Calif. School of Law 715, 730-31 (1954), quoting Member Sternhagen, dissenting in *Burroughs Bldg. Material Co.*, 18 B. T. A. 101, 105 (1929), aff'd, 47 F. 2d 178 (2d Cir. 1931). (Footnotes omitted.)

[9] See, e.g., *National Outdoor Advertising Bureau* v. *Helvering*, 89 F. 2d 878, 880-81 (2d Cir. 1937).

[10] See, e.g., *Burroughs Bldg. Material Co.* v. *Commissioner*, 47 F. 2d 178 (2d Cir. 1931).

missioner v. *Heininger*, 320 U. S. 467, 470, 471, 472 (1943):

> "There can be no doubt that the legal expenses of respondent were directly connected with 'carrying on' his business. . . .
>
> "It is plain that respondent's legal expenses were both 'ordinary and necessary" if those words be given their commonly accepted meaning. For respondent to employ a lawyer to defend his business from threatened destruction was 'normal'; it was the response ordinarily to be expected. Cf. *Deputy* v. *du Pont*, 308 U.S. 488, 495 [1940]; *Welch* v. *Helvering*, 290 U.S. 111, 114 [1933]; *Kornhauser* v. *United States*, [276 U. S. 145 (1928)] . . . Since the record contains no suggestion that the defense was in bad faith or that the attorney's fees were unreasonable, the expenses incurred in defending the business can also be assumed appropriate and helpful, and therefore 'necessary.' . . .
>
> "To say that . . . the expenses . . . were extraordinary or unnecessary would be to ignore the ways of conduct and the forms of speech prevailing in the business world."

To the extent that the equation of illegality with extraordinary and unnecessary is not question begging, it is applying special meanings to "ordinary and necessary" which are not applied in other connections. So long as the expense arises out of the conduct of the business and is a required outlay it ought to be considered ordinary and necessary.

[fol. 41] As to public policy the Supreme Court held in *Lilly* v. *Commissioner*, 343 U. S. 90, 96-97 (1952).

> "Assuming for the sake of argument that, under some circumstances, business expenditures which are ordinary and necessary in the generally accepted meanings of those words may not be deductible as 'ordinary and necessary' expenses under § 23(a)(1)(A) [Section 162(a)] when they 'frustrate sharply defined national or state policies proscribing particular types of conduct,' . . . nevertheless the expendi-

tures now before us do not fall in that class. The policies frustrated must be national or state policies evidenced by some governmental declaration of them." [11]

There has been no "governmental declaration" of any "sharply defined" national or state policy or discouraging the hiring of counsel and the incurring of other legal expense in defense against a criminal charge. In fact it is highly doubtful whether such a public policy could exist in the face of the Sixth Amendment's guaranty of the right to counsel.[12]

[fol. 42] The rule of disallowance of legal expenses in the case of unsuccessful defenses has been adversely criticized by numerous commentators.[13]

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[11] Quoting *Commissioner* v. *Heininger*, 320 U.S. at 473. See also *Tank Truck Rentals, Inc.* v. *Commissioner*, 356 U. S. 30 (1958); *Commissioner* v. *Sullivan*, 356 U. S. 27 (1958).

[12] See *Powell* v. *Alabama*, 287 U. S. 45, 68-69 (1932):

"The right to be hear would be, in many cases, of little avail if it did not comprehend the right to be heard by counsel. Even the intelligent and educated layman has small and sometimes no skill in the science of law. If charged with crime, he is incapable, generally, of determining for himself whether the indictment is good or bad. He is unfamiliar with the rules of evidence. Left without the aid of counsel he may be put on trial without a proper charge, and convicted upon incompetent evidence, or evidence irrelevant to the issue or otherwise inadmissible. He lacks both the skill and knowledge adequately to prepare his defense, even though he have a perfect one. He requires the guiding hand of counsel at every step in the procedings against him. Without it, though he be not guilty, he faces the danger of conviction because he does not know how to establish his innocence."

[13] See, e.g., Arent, *Inequities in Non-Deductibility of Fines, Penalties, Defense Expense*, 87 J. Accountancy 482, 485-86 (1949); Brookes, *Litigation Expenses and the Income Tax*, 12 Tax L. Rev. 241 (1957); Keesling, *Illegal Transactions and the Income Tax*, 5 U. C. L. A. L. Rev. 26, 33-40 (1958); Paul, *supra* note 7; Reid, *Disallowance of Tax Deductions on Grounds of Public Policy—a Critique*, 17 Fed. B. J. 575 (1957); Stapleton, *The Supreme Court Redefines Public Policy* 41 Taxes 641 (1952); Note, *Public Policy and Federal Income Tax Deductions*, 51 Colum. L. Rev. 752, 756-58 (1951); Note, *Deduction of Business Expenses: Illegality and*

Adherence to the rule has led to anomalous, arbitrary, artificial and conflicting results. The attempt to apply a rule which seeks to distinguish between civil and criminal liability and successful and unsuccessful defenses has caused repeated difficulty in borderline cases. A disbarment proceeding, for example, has been classified as criminal and the legal expenses disallowed.[14] Legal expenses paid in behalf of an employee who was found guilty of violating certain sections of the California administrative code relating to horse-racing and who, as a result, lost his license as a trainer, were held deductible, but the court said that had the employee paid his own expenses they "probably" would not have been deductible by him.[15] A taxpayer was permitted to deduct attorney's fees in connection with settlement of a civil liability for assault,[16] while another taxpayer's legal expenses in defending an action for defrauding the government were disallowed.[17] [fol. 43)] When the taxpayer finally pleaded *nolo contendere*, the legal expenses of an unsuccessful trial and a successful appeal (i.e., successful in securing a new trial) were disallowed.[18] Legal fees expended in an unsuccessful attempt to avoid a prosecution resulting in conviction are not deductible.[19] Where a taxpayer pleaded *nolo contendere* to an indictment for tax evasion and the Tax Court later found that there was no fraud or fraudulent evasion for the years in question, the legal expenses connected with the indictment were held to be non-deduct-

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Public Policy, 54 Harv. L. Rev. 852, 854-57 (1941); Comment, *Business Expenses, Disallowances, and Public Policy*, 72 Yale L. J. 108, 132-36 (1962).

[14] *Estate of G. A. Buder*, T. C. Memo. 1963-73, 22 CCH Tax Ct. Mem. 300, aff'd on other issues, 330 F. 2d 441 (8th Cir. 1964).

[15] *Robert S. Howard*, 32 T. C. 1284, 1296 (1959).

[16] *John W. Clark*, 30 T. C. 1330 (1958).

[17] *David R. Faulk*, 26 T. C. 948 (1956).

[18] *Standard Coat, Apron & Linen Serv.*, 40 T. C. 858 (1963).

[19] *Tracy* v. *United States*, 284 F. 2d 379 (Ct. Cl. 1960). *But see Commissioner* v. *Schwartz*, 232 F. 2d 94 (5th Cir. 1956).

ible.[20] On the other hand, legal expenses in connection with an unsuccessful defense against civil liability for taxes are deductible even where a fraud penalty is assessed.[21] The Commissioner disallows legal expenses in government actions under the antitrust laws but allows deduction of such expenses in private actions.[22]

This is the first occasion that we have had since *Heininger* and *Lilly* to reexamine our rule as to deductibility of legal expenses for an unsuccessful defense connected with the carrying on of a trade or business. We hold, following *Heininger*, that such expenses are ordinary and necessary within the meaning of the statute. We find no sharply defined public policy against the allowance of such deductions, as is required by *Lilly*. We therefore refuse to continue to draw any distinction in deductibility between civil and criminal cases or between successful and unsuccessful defenses. We hold that legal expenses are deductible where they arise out of and are immediately or [fol. 44] proximately connected with, and are required for, the conduct of a trade or business.

Reversed.

MOORE, *Circuit Judge*, took no part in the consideration or decision of this case.

LUMBARD, *Chief Judge*, with whom WATERMAN and KAUFMAN, *Circuit Judges*, join (concurring):

While concurring in Judge Hays' opinion for the court, I wish to add a brief word. In our decision in *Burroughs Bdg. Material Co.* v. *Commissioner*, 47 F. 2d 178, 180 (1931), we disallowed expenses incurred in the unsuccessful defense of criminal charges on the ground that to do so would be contrary to public policy. In my opinion,

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[20] *Bell* v. *Commissioner*, 320 F. 2d 953 (8th Cir. 1963).

[21] *Hopkins* v. *Commissioner*, 271 F. 2d 166 (6th Cir. 1959).

[22] Rev. Rul. 64-224, 1964 Int. Rev. Bull. No. 33, at 13.

there is no present basis for the claim that such disallowance is consistent with public policy; on the contrary, it seems clear to me that public policy now requires us to allow the deduction.

Since *Burroughs* was decided, the federal courts have given fuller meaning to the Sixth Amendment, which guarantees to every defendant the right to be represented by counsel.

In 1938 the Supreme Court held in *Johnson* v. *Zerbst*, 304 U. S. 458, that counsel must be furnished an accused who is financially unable to retain his own counsel to defend him on federal charges. A few months ago Congress at long last realized that the right to counsel has little substance unless counsel is paid for his efforts and reimbursed for necessary expenses. Under the provisions of the Criminal Justice Act, 18 U. S. C. § 3006(a), which became law on August 20, 1964, a defendant who is found to be financially unable to provide counsel and defray de- [fol. 45] fense expenses is now entitled to have such reasonable and necessary expenses paid by the government up to specified maximum amounts.

The assignment and compensation of counsel under the Criminal Justice Act do not depend on whether a defendant successfully asserts his innocence. Indeed, almost all of counsel's labors ordinarily must be done and his expenses must be incurred before guilt or innocence is finally established. The defendant has the right to put the government to its proof, if he so elects. His right to counsel does not depend upon whether in fact he has a defense or whether it was reasonable to contest the charges. Surely it needs no argument to support the proposition that unless a defendant has the benefit of counsel who can give necessary attention to the charges and their defense—and in cases such as Tellier's, this is usually a considerable task for conscientious counsel—he may not be in a position to make an intelligent and knowing decision as to whether or how to conduct a defense. Moreover, whether he stands trial or pleads guilty, he needs counsel who has thoroughly familiarized himself with the case and who can plead for his client in the light of such knowledge. If the compensation of counsel under the Criminal Justice

Act does not depend on the success of the defense, it would seem to follow that the allowance of the deduction should not depend on the outcome in cases where the defendant is able to and does assume the financial burden of defending against criminal charges.

In holding that a financially able defendant may deduct as "ordinary and necessary" expenses the legal fees and expenses incurred in an unsuccessful defense, we are being consistent with a clearly evinced policy that a defendant be represented by counsel regardless of the ultimate success or failure of his defense.

[fol. 46] As there is no provision of the tax laws which requires a contrary result, I agree that we should not impose an additional penalty on financially able defendants by refusing a deduction in such cases. The allowance of the deduction here sought is consonant with public policy and ought to be allowed. I think the teaching of *Johnson* v. *Zerbst, supra, Gideon* v. *Wainwright*, 372 U. S. 335 (1963), and the Criminal Justice Act requires this result and that we are no longer bound by *Burroughs*.

WATERMAN, *Circuit Judge* (concurring):

I concur in Judge Hays' opinion and I also concur in Chief Judge Lumbard's additional separate concurrence.

KAUFMAN, *Circuit Judge* (concurring):

I concur in the opinions of both Judge Hays and Chief Judge Lumbard.

[fol. 47]

IN THE UNITED STATES COURT OF APPEALS
FOR THE SECOND CIRCUIT

* * * *

Present:

HON. J. EDWARD LUMBARD, Chief Judge,
HON. STERRY R. WATERMAN,
HON. HENRY J. FRIENDLY,
HON. J. JOSEPH SMITH,
HON. IRVING R. KAUFMAN,
HON. PAUL R. HAYS,
HON. THURGOOD MARSHALL,
HON. ROBERT P. ANDERSON,
Circuit Judges.

WALTER F. TELLIER AND EVELYN H. TELLIER,
PETITIONERS

v.

COMMISSIONER OF INTERNAL REVENUE, RESPONDENT

JUDGMENT—February 16, 1965

Appeals from The Tax Court of the United States.

This cause came on to be heard on the transcript of record from The Tax Court of the United States, and was argued by counsel.

ON CONSIDERATION WHEREOF, it is now hereby ordered, adjudged, and decreed that the order of said The Tax Court of the United States be and it hereby is affirmed in part and reversed in part in accordance with the opinions of this court.

A. DANIEL FUSARO
Clerk

[fol. 48]

[File Endorsement Omitted]

[fol. 49]

[Clerk's certificate to foregoing
transcript omitted in printing]

[fol. 50]

SUPREME COURT OF THE UNITED STATES

* * * *

ORDER EXTENDING TIME TO FILE PETITION FOR WRIT OF CERTIORARI—May 19, 1965

UPON CONSIDERATION of the application of counsel for petitioner,

IT IS ORDERED that the time for filing a petition for writ of certiorari in the above-entitled case be, and the same is hereby, extended to and including June 16, 1965.

/s/ John M. Harlan
Associate Justice of the
Supreme Court of the United States

Dated this May 19th, 1965

[fol. 51]

SUPREME COURT OF THE UNITED STATES

* * * *

ORDER EXTENDING TIME TO FILE PETITION FOR WRIT OF CERTIORARI—June 17, 1965

UPON CONSIDERATION of the application of counsel for petitioner,

IT IS ORDERED that the time for filing a petition for writ of certiorari in the above-entitled case be, and the same is hereby further extended to and including July 16, 1965.

/s/ John M. Harlan
Associate Justice of the
Supreme Court of the United States

Dated this 17th day of June, 1965

[fol. 52]

SUPREME COURT OF THE UNITED STATES

No. 351, October Term, 1965

COMMISSIONER OF INTERNAL REVENUE, PETITIONER

v.

WALTER F. TELLIER, ET UX

ORDER ALLOWING CERTIORARI.—October 11, 1965.

The petition herein for a writ a certiorari to the United States Court of Appeals for the Second Circuit is granted; and the case is placed on the summary calendar.

And it is further ordered that the duly certified copy of the transcript of the proceedings below which accompanied the petition shall be treated as though filed in response to such writ.

☆ U. S. GOVERNMENT PRINTING OFFICE: 1965 792004 304